

~~STATE OF SOUTH CAROLINA)~~

VERIFICATION

COUNTY OF UNION )

PERSONALLY appeared before me, Paul W. Inman, who being duly sworn states:

That he is the Business Controller of Lockhart Power Company; that the testimony attached hereto as Testimony of Paul W. Inman is based upon information that he believes to be true and correct.

  
Paul W. Inman

Sworn to before me this  
22<sup>nd</sup> day of December, 2010

  
Rabecka Chavis

My Commission Expires: Jan. 14, 2019

**Testimony of Paul W. Inman  
Docket Number 2010-181-E**

1    **Q.    PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2    **A.    Paul W. Inman, Lockhart Power Company, Post Office Box 10, Lockhart, South**  
3           **Carolina 29364.**

4    **Q.    PLEASE STATE YOUR PRESENT POSITION.**

5    **A.    I am Business Controller of Lockhart Power Company.**

6    **Q.    WHAT IS YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL**  
7           **EXPERIENCE?**

8    **A.    I hold a Bachelor of Arts degree in Business Administration from Limestone**  
9           **College. I also hold a Master of Business Administration degree from the**  
10          **University of South Carolina. I was employed by Lockhart Power Company in**  
11          **1972 as a Management Trainee. Later that same year I was promoted to**  
12          **Business Controller of Lockhart Power Company.**

13   **Q.    WILL YOU BRIEFLY SUMMARIZE YOUR DUTIES AND RESPONSIBILITIES**  
14          **WITH LOCKHART POWER COMPANY?**

15   **A.    I have complete responsibility for all accounting and financial reporting aspects of**  
16          **Lockhart Power Company.**

17   **Q.    WOULD YOU PLEASE DESCRIBE THE PURPOSE OF YOUR TESTIMONY?**

18   **A.    I will discuss certain accounting adjustments and accounting proforma**  
19          **adjustments made to the test year in this filing, and will discuss the deferred**  
20          **revenue aspect of our Power Adjustment Clause.**

## Testimony of Paul W. Inman

### Docket Number 2010-181-E

1 Q. WOULD YOU PLEASE DESCRIBE CERTAIN ACCOUNTING ADJUSTMENTS  
2 AND ACCOUNTING PROFORMA ADJUSTMENTS THAT WERE MADE TO  
3 THE TEST YEAR IN THIS FILING?

4 A. Lockhart Power Company ("Lockhart Power Company" or "Company") made  
5 adjustments to beginning (12-31-09) book balances for certain revenue and  
6 expense accounts to remove the effect of non-jurisdictional contracts before  
7 beginning the process of proforma adjustments. Sales of hydro generation were  
8 made off-system and recorded in the appropriate FERC revenue account.  
9 Associated expenses were also made and recorded in the appropriate expense  
10 accounts. These amounts, being non-jurisdictional, were removed from the  
11 consolidated revenue and expense account values as reported in the FERC  
12 Form 1 to yield adjusted balances from which to begin proforma adjustments.  
13 Proforma adjustments were then made to certain test year revenues, expenses  
14 and rate base balances to normalize these values by either adjusting for known  
15 changes, or to adjust abnormal revenues or expenses to an appropriate normal  
16 annual level. The individual proforma adjustments are described below.

#### 17 Electric Plant Adjustments

18 In order to use a current level of electric fixed assets in the development of this  
19 filing, the Company included in its rate base Electric Plant in Service and  
20 Construction Work in Progress balances as of July 31, 2010. In addition,  
21 adjustments were made to Electric Plant to account for certain known and  
22 measurable capital-related changes that will occur after July 31, 2010, assuming

## **Testimony of Paul W. Inman**

### **Docket Number 2010-181-E**

1 Commission approval. Specifically, the Company has made a binding capital  
2 commitment of \$1,510,000 for the purchase of a City of Union diesel peaking  
3 plant to occur after July 31, 2010. The scheduled closing date for that purchase  
4 is not later than May 31, 2011. Final investment in the plant purchase is  
5 expected to total \$1,519,804 plus closing expenses. A series of accounting  
6 proforma adjustments were made to the book values at July 31, 2010 to reflect  
7 the actual cost of Plant in Service of \$2,473,171 and Accumulated Depreciation  
8 of \$507,339, as of the date of the purchase. Because the purchase price is  
9 below the net book value, an additional credit adjustment was made to  
10 Accumulated Depreciation in the amount of \$446,028 to adjust the net book  
11 value of the acquired plant down to the actual cost of the investment. This  
12 results in total Accumulated Depreciation increase adjustments resulting from the  
13 diesel peaking plant of \$953,367.

14  
15 The Company has also made a significant investment in a landfill gas to power  
16 plant that is presently under construction at the Wellford Landfill in Spartanburg  
17 County, South Carolina. This plant will effectively reduce Lockhart Power's cost  
18 of purchased power that is flowed through to its customers. As of July 31, 2010,  
19 the Company had made capital expenditures totaling \$2,475,500 as a part of this  
20 construction project. Inasmuch as it is expected that this project will be  
21 completed at or near the time this rate proceeding is finalized, the costs incurred  
22 through July 31, 2010 are effectively reclassified from Construction Work in

## Testimony of Paul W. Inman

### Docket Number 2010-181-E

1 Progress to Electric Plant in Service. (SEE EXHIBIT A3-8 PROFORMA –  
2 UTILITY PLANT WORKSHEET)

#### 3 Depreciation Expense Annualization

4 The Company has made a proforma adjustment to annualize its Depreciation  
5 Expense, because the test year actual depreciation expense does not consider  
6 the effect of certain known and measurable changes that should be taken into  
7 account. First, provisions for depreciation on capital expenditures made during  
8 the test year occurred as the assets went into service throughout the year. This  
9 resulted in only a partial year of depreciation expense in the test year on those  
10 additions, which is annualized as a proforma adjustment. Second, plant in  
11 service and accumulated depreciation as of July 31, 2010 are now included in  
12 rate base. Therefore, annual depreciation expense attributable to those capital  
13 additions occurring between December 31, 2009 and July 31, 2010 must also be  
14 included. Finally, the diesel peaking plant purchase and the landfill gas to  
15 electric energy plant construction projects, the costs of which were either spent  
16 or committed to be spent after July 31, 2010, are being included in rate base.  
17 Consequently, depreciation expense has been herein normalized to reflect a  
18 whole year of depreciation on the total plant included in rate base. Depreciation  
19 and amortization expenses per books for the test year amounted to \$1,302,242.  
20 Considering the above adjustments to plant, depreciation and amortization  
21 expenses were recalculated, applying annual rates to the adjusted ending plant  
22 balances. This resulted in total depreciation and amortization expenses of

## **Testimony of Paul W. Inman**

### **Docket Number 2010-181-E**

1       \$1,545,960. Therefore, an adjustment is herein made to increase test year  
2       Depreciation Expense by \$243,718. A corresponding adjustment is made to  
3       increase test year accumulated depreciation by this same amount of \$243,718.

4       (SEE EXHIBIT A3-9 PROFORMA DEPRECIATION & AMORTIZATION  
5       WORKSHEET)

#### **Property Tax Expense Annualization**

7       Property taxes for the test year were understated on a prospective basis due to  
8       three categories of changes in capital expenditures for which no property taxes  
9       were included. These were as follows: (1) capital expenditures made during the  
10      test year (2) capital expenditures made between December 31, 2009 and July  
11      31, 2010, and (3) special capital expenditures either made or committed to be  
12      made after July 31, 2010. Actual property tax expense in the test year was  
13      based on plant in service as of December 31, 2008. Therefore, property taxes  
14      attributable to the above additional three categories of capital expenditures  
15      should be added to test year expense to normalize the cost. A calculation of  
16      property-related taxes using the revised investment level yields an adjusted total  
17      annual cost of \$879,006. Actual property-related tax expenses included in the  
18      test year amounted to \$665,441. Test year Property Tax Expense is therefore  
19      adjusted by \$213,565. (SEE EXHIBIT A3-10 PROFORMA PROPERTY-  
20      RELATED TAX ADJUSTMENT WORKSHEET)

#### **City of Union Diesel Peaking Plant Operating Expense**

## **Testimony of Paul W. Inman**

### **Docket Number 2010-181-E**

1 As referred to above under Electric Plant Adjustments, the Company has entered  
2 into a contract to purchase a 7300 kW diesel peaking facility from the City of  
3 Union, South Carolina. This facility will reduce the Company's purchased power  
4 expense by the value of the power generated. The operation of this facility will  
5 incur certain ongoing operating and maintenance costs. Based on Lockhart  
6 Power's experience operating its own diesel peaking plant, which has very  
7 similar operating characteristics to the subject plant, these costs are projected to  
8 be \$97,843 annually. Test year expense is therefore adjusted by \$97,843 to  
9 include these additional costs. (SEE EXHIBIT A3-11 PROFORMA – CITY  
10 DIESEL PLANT OPERATING EXPENSE WORKSHEET)

#### **Wellford Landfill Gas Operating and Maintenance Expense**

12 As referred to above under Electric Plant Adjustments, during 2010 the Company  
13 has made a significant investment in a landfill gas to power plant that is located  
14 at the Wellford Landfill in Spartanburg County, South Carolina. In addition to the  
15 capital expenditures referred to above, the operation of this facility will also incur  
16 certain ongoing operating and maintenance costs. These costs are projected to  
17 be \$256,164 annually and are comprised mainly of methane gas purchases,  
18 scheduled preventive maintenance, labor and insurance expenses. The test  
19 year expense is therefore adjusted by \$256,164 to include these costs. (SEE  
20 EXHIBIT A3-12 PROFORMA – WELLFORD LANDFILL GAS OPERATING &  
21 MAINTENANCE EXPENSE WORKSHEET)

#### **Purchased Power Expense Adjustment**

## **Testimony of Paul W. Inman**

### **Docket Number 2010-181-E**

1 An adjustment has been made to Purchased Power Expense to include the effect  
2 of four structural changes that have been made that impact this account. First,  
3 upon the completion of the transaction whereupon Lockhart Power will purchase  
4 the diesel peaking plant from the City of Union, the Company should realize an  
5 average reduction in its annual purchased power cost of \$802,217. This  
6 reduction arises from the use of the plant to shave the annual peak demand that  
7 Lockhart places on Duke Energy's system. The peak shaving process is already  
8 in place, but the benefit presently accrues to the shareholder, since the cost is  
9 not included in rates at this time. Upon approval and execution of the plant  
10 purchase, the costs and benefits of ownership will begin to flow through to the  
11 customer. The test year is therefore adjusted to reduce Purchased Power  
12 Expense by \$802,217 to reflect the reduction in the annual cost. Second,  
13 Purchased Power Expense per books for the test year included \$140,786 of cost  
14 associated with the shareholder benefit stated above that should properly be  
15 removed from cost of service, and which will be non-recurring after Lockhart  
16 owns the diesel peaking plant. Test year Purchased Power Expense is therefore  
17 adjusted to remove this cost from the annual total expense.

18  
19 Third, Duke Energy entered a new wholesale contract with Lockhart Power  
20 Company on January 1, 2009, the terms of which included the application of a  
21 formula rate. Under this structure, charges were billed by Duke throughout the  
22 current year based on beginning-of-year estimates of demand and energy rates



## Testimony of Paul W. Inman

### Docket Number 2010-181-E

1 and demand units. A true-up adjustment would be made during the next year  
2 after all actual costs and billing units were known. Such was the handling of  
3 Lockhart's billing for Purchased Power costs during test year 2009 and the  
4 ensuing 2010 year. During 2010, Duke credited Lockhart Power Company with  
5 true-up credit adjustments over a 5-month period. These credit adjustments  
6 were immediately flowed through to Lockhart's customers via its Purchased  
7 Power Adjustment Clause (Schedule O) in the next month after receiving each  
8 credit adjustment. Inasmuch as these credits were for over-estimated charges  
9 made during the test year, the test year 2009 costs should be reduced to reflect  
10 the true-up. Therefore, an adjustment is herein made to reduce Purchased  
11 Power Expense accordingly for this true-up in the amount of \$1,445,686. Fourth,  
12 in early 2010, one of Lockhart Power Company's oldest and largest industrial  
13 customers ceased its manufacturing operations and closed the plant. Much of  
14 the power used by this plant was supplied through purchases by Lockhart from  
15 Duke Energy. Since these sales will not recur prospectively, the associated  
16 Purchased Power Expense will also be non-recurring. Therefore, test year  
17 Purchased Power Expense is herein reduced accordingly in the amount of  
18 \$833,929 to normalize expense for the lost customer. The net effect of these  
19 four changes is an annual reduction in purchased power expense of \$3,222,618.  
20 (SEE EXHIBIT A3-13 PROFORMA – PURCHASED POWER EXPENSE  
21 WORKSHEET)Wage Increase Annualization

## Testimony of Paul W. Inman

### Docket Number 2010-181-E

1 An average wage increase of 2.24% became effective on employee earnings  
2 occurring on or after November 27, 2009. It was further anticipated that an  
3 average wage increase of 2.83% would become effective on all employee  
4 earnings occurring on or after November 28, 2010. A calculation was made to  
5 determine the effect of including the 2.24% increase for the whole test year,  
6 which amounts to a gross additional cost of \$38,202 for the 47 weeks from  
7 January 1, 2009 to November 27, 2009. A different calculation was made for the  
8 second wage increase, which became effective November 28, 2010, in order to  
9 account for its annual impact as well. The annual effect of this second scheduled  
10 wage adjustment amounted to \$57,595 (The actual final adjustment amounted to  
11 approximately 3.6%, although the lower estimated amount had already been  
12 included in the proforma adjustment). The two adjustments taken as a total,  
13 amounted to \$95,797. This total was further broken down into rate base and  
14 expense components and amounted to \$18,451 and \$77,346 respectively. A  
15 rate base increase of \$18,451 was therefore made for the capitalized portion of  
16 the wage adjustment. An adjustment to increase expense was made in the  
17 amount of \$77,346. (SEE SEE EXHIBIT A3-14 PROFORMA - WAGE  
18 INCREASE ANNUALIZATION WORKSHEET)

#### Employee Count Adjustment

20 Between the end of the Test Year 2009 and before the implementation of new  
21 rates, certain changes have been made resulting in employee complement  
22 additions for new hires. These consist of an Assistant Business Controller and

## Testimony of Paul W. Inman

### Docket Number 2010-181-E

1 an Assistant Transmission & Distribution Manager. These two complement  
2 additions resulted in a total increase in annual salaries cost of approximately  
3 \$150,000 and were included at that amount. The test year data is also  
4 understated by amounts resulting from one employee having been on military  
5 leave for most of the test year, and for another employee who was hired near the  
6 end of the test year. An annualization of these two employees' earnings will  
7 result in an additional \$36,724 and \$15,779 respectively. When added together  
8 with the two complement additions referred to earlier, the additional wages  
9 adjustment to the test year will amount to a total of \$202,503. Based on  
10 company salaries & wages experience for the test year, the breakdown of this  
11 total will amount to \$39,002 for the capital component and \$163,501 for the  
12 expense portion. Adjustments to increase rate base and expense respectively by  
13 these amounts are therefore included. (SEE EXHIBIT A3-15 PROFORMA –  
14 EMPLOYEE COUNT ADJUSTMENT WORKSHEET)

#### 15 Fringe Benefits Annualization

16 The gross amounts of the two wage increase annualization adjustments as  
17 described above are \$38,202 and \$57,595 respectively, for a total of \$95,797.  
18 The gross amount of the employee count adjustment as also described above is  
19 \$202,503. The total amount of these two wage-related proforma adjustments  
20 added together is \$298,300. Variable fringe benefits costs during the test year  
21 amounted to 15.94% of direct earnings, which would result in an additional fringe  
22 benefits expense of \$47,549. This amount is therefore reflected as an

## Testimony of Paul W. Inman

### Docket Number 2010-181-E

adjustment to expense. (SEE EXHIBIT A3-16 PROFORMA – FRINGE BENEFITS ON EARNINGS - RELATED ADJUSTMENTS WORKSHEET)

#### Transmission System Study Expense

The Company had a study of its Transmission system performed to evaluate its overall capacity and reliability. This was prompted by the need for flexibility and emergency switching capabilities in providing power to the local industrial park and surrounding communities. Adding to the urgency of this situation, one of Lockhart Power's industrial customers began plans for a major expansion of its operations. Lockhart Power subsequently began planning for the addition of a new transmission line as recommended by the study. However, the industrial expansion did not materialize to the degree anticipated. Simultaneously, another major industrial customer announced plans to begin phasing out its operations. This effectively eliminated the need for a system expansion by Lockhart. Consequently, the cost of the study was written off to expense in the test year and must be normalized. Proforma adjustments are made as follows: (1) the cost of the study, which was written off during 2009 and amounted to \$162,537, was removed from test year G&A expense, and (2) this cost is herein amortized over a 2-year period by the inclusion of an increase adjustment to G&A expense of \$81,269. (SEE EXHIBIT A3-17 PROFORMA - TRANSMISSION SYSTEM STUDY EXPENSE WORKSHEET)

#### Rate Case Expense Amortization

## **Testimony of Paul W. Inman**

### **Docket Number 2010-181-E**

1 Professional services and other administrative costs incurred in connection with  
2 this rate application are expected to amount to \$113,000. This amount is herein  
3 amortized over 2 years, or \$56,500 per year as an increase to expense. The  
4 test year also included prior rate case expense amortization of \$30,217.  
5 Amortization of the prior case ended July 31, 2010. Consequently, a proforma  
6 adjustment is made to reduce test year rate case expense by the non-recurring  
7 amortization amount of \$30,217. (SEE EXHIBIT A3-18 PROFORMA – RATE  
8 CASE EXPENSE WORKSHEET)

#### **Training Grant Credit Removal**

9  
10 During 2009, Lockhart Power Company received certain training grant payments  
11 which were accounted for as offsets against on-the-job training of new  
12 employees by existing employees. These grants were one-time events involving  
13 new employees, but had no incremental costs associated. The credits are herein  
14 removed from the test year by an increase adjustment to expense. (SEE  
15 EXHIBIT A3-19 PROFORMA – TRAINING GRANT CREDIT REMOVAL  
16 WORKSHEET)

#### **Industrial Revenue Reduction for Monarch Plant Closing**

17  
18 In early 2010, one of Lockhart Power Company's oldest and largest industrial  
19 customers ceased its manufacturing operations and closed the plant (See  
20 comments under Purchased Power Expense Adjustment summary above).  
21 Sales to this customer during the test year totaled \$1,047,722. These sales will  
22 be non-recurring prospectively, and are therefore removed from the 2009 test

## Testimony of Paul W. Inman

### Docket Number 2010-181-E

1 year revenues. (SEE EXHIBIT A3-20 PROFORMA – INDUSTRIAL REVENUE  
2 REDUCTION FOR MONARCH PLANT CLOSING WORKSHEET)

#### 3 Wellford Landfill Gas Sales Adjustments

4 Lockhart Power's Wellford Landfill Gas to Electric Energy facility is scheduled to  
5 begin operations in early 2011. The sale of output from this plant will be made  
6 off-system at negotiated contract prices. Sales are expected to average  
7 \$643,741 annually over the next two (2) years. The entire proceeds of these  
8 sales will be credited back to Lockhart's requirements customers as a reduction  
9 of their revenue requirement via the Company's Power Adjustment Clause. This  
10 will result in a greater benefit to the customer than would have resulted had the  
11 power been sold internally, thus avoiding only the incremental cost of the  
12 reduced purchased power at the wholesale rate. It is necessary that two  
13 adjustments be made to test year 2009 revenues to properly reflect the impact of  
14 these sales and their special treatment. First, an adjustment is made to increase  
15 sales by \$643,741 to account for the off-system wholesale transaction.  
16 Secondly, an adjustment is made to decrease jurisdictional sales by an off-  
17 setting \$643,741 to reflect the pass-through of the proceeds of the sales to  
18 requirements customers via the Company's Power Adjustment Clause. (SEE  
19 EXHIBIT A3-21 PROFORMA – WELLFORD LANDFILL GAS SALES)

20 Q. WOULD YOU EXPLAIN WHY THERE WILL BE A DEFERRED BILLING OF  
21 POWER COST EXPENSE AT THE TIME NEW RATES TAKE EFFECT?

**Testimony of Paul W. Inman**  
**Docket Number 2010-181-E**

1   **A.**   Lockhart Power Company's Rate Schedule O provides for the pass-through to  
2       the customer of any increases above or decreases below the base cost of  
3       Purchased Power and fuel used for generation, less applicable wholesale power  
4       sales, per kWh sold. The net total cost of these categories is calculated for each  
5       month and compared to the base cost of such items that is included in the  
6       Company's base electric rates. Any variation in the monthly cost from the base  
7       amount (after being adjusted for gross receipts tax) is passed on to the customer  
8       during the following month. This adjustment can be either positive or negative. If  
9       positive, the customer will receive a charge on the billing. If negative, a credit will  
10      be applied to the billing. At the time new rates take effect, there will be a one-  
11      month over or under recovery of Purchased Power cost under the old rates that  
12      will be trued up in the following month. (Note: under the old rates, Purchased  
13      Power was the only cost included under Rate Schedule O)

14   **Q.**   **DOES THIS CONCLUDE YOUR TESTIMONY?**

15   **A.**   Yes.